



Apple trees, 1973. Detail. By Michael Archer, one of the Skagen Painters. This image belongs to the Art Museums of Skagen.

# SKAGEN Credit EUR

## Status report May 2017

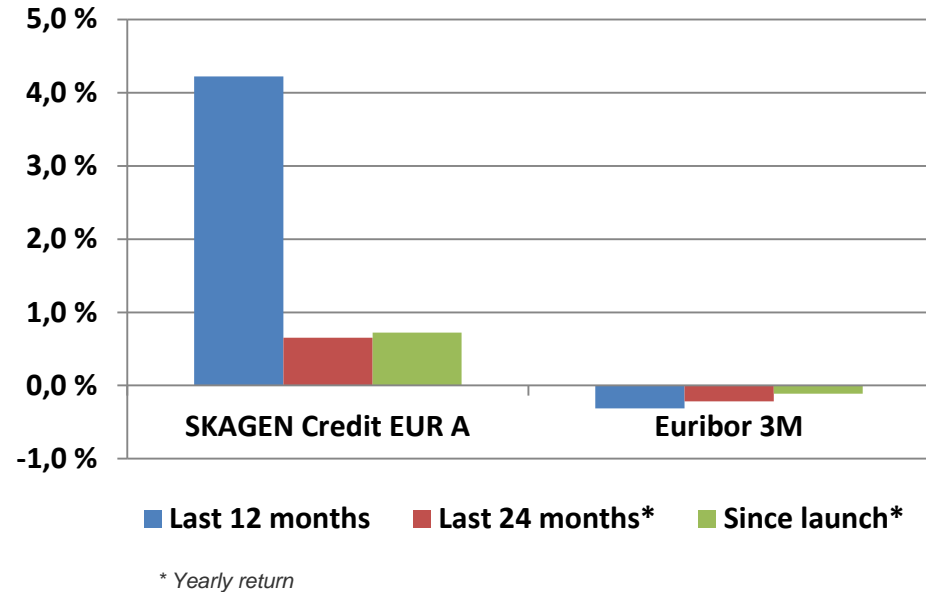
The art of common sense

**3Y EDITION**



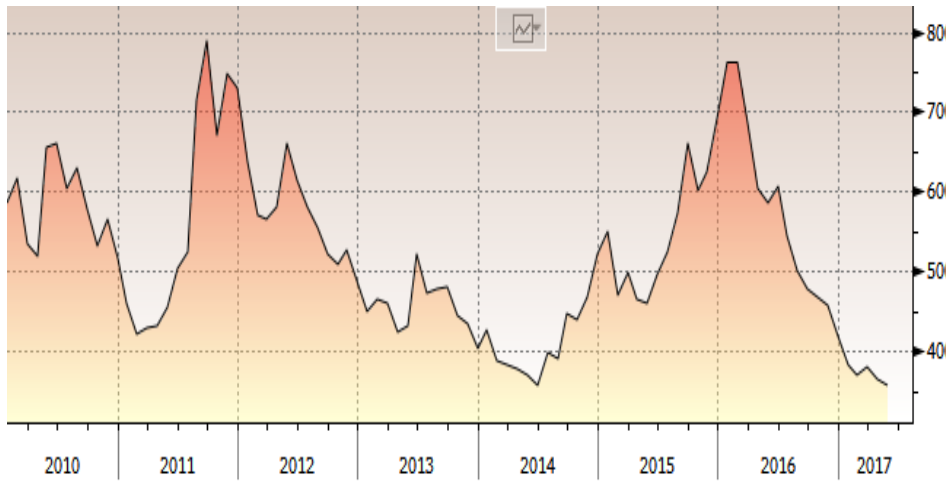
# 3Y SKAGEN Credit EUR – three year anniversary

- Good performance
- A unique mandate that works according to plan
- The fund's flexible mandate makes it well positioned for the future



# 3Y Corporate bonds over the past three years

The past three years have seen some rather significant changes in corporate bond prices. When the fund was launched back in May 2014, global corporate bonds were trading at historically low spreads. This is illustrated below in the graph showing the average risk premium global that “high yield” corporates pay in the fixed income market.



*Bloomberg Global High Yield Corporate Bond Index*

Unfortunately the dip in mid-2014 coincides with the launch of SKAGEN Credit. Increasing credit spreads caused bond prices to decrease, so the latter part of 2014 was not a favourable period when spreads increased.

Bond spreads increased again towards the end of 2015 and continued to do so until early 2016. The extreme levels were reversed rather quickly and the remainder of 2016 was pleasant with continuously lower spreads.

In 2017 this spread decrease has continued and corporate bond spreads are now back on a par with May 2014.

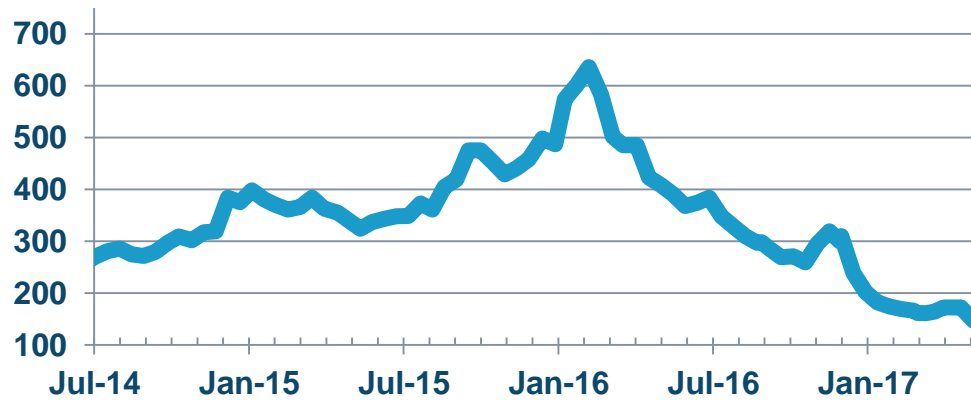
## 3Y Credit spread in the fund

The previous slide discussed the corporate bond spread on a general level. This leads us on to why it is important that SKAGEN Credit is not an index fund but rather has the flexibility to pick corporate bonds from all around the world. The fund holds a fairly concentrated portfolio of around 40 holdings.

The credit spread on a single bond changes when the issuing company's credit quality changes. If a company for example raises more equity, the equity/debt ratio improves and the risk decreases for the bond holders. The company's business situation can also improve and thereby its future earnings, resulting in a lower risk for bond holders. Such changes are what we look for when picking bonds in SKAGEN Credit. By constantly picking the "right bonds" the fund will in the long run generate a better return than investing in the broad index.

During periods of significant changes to the average level, improvements in a single company's credit metrics have little impact. When a whole sector is shunned for some reason or another, all bonds' spreads change more or less in line with one another. The average spread on the holdings in the fund changes with the market and it is therefore important to look at general levels.

The graph to the right shows the average credit spread in SKAGEN Credit but doesn't say anything about the risk-level of the underlying bonds.



Average credit spread in SKAGEN Credit (OAS)

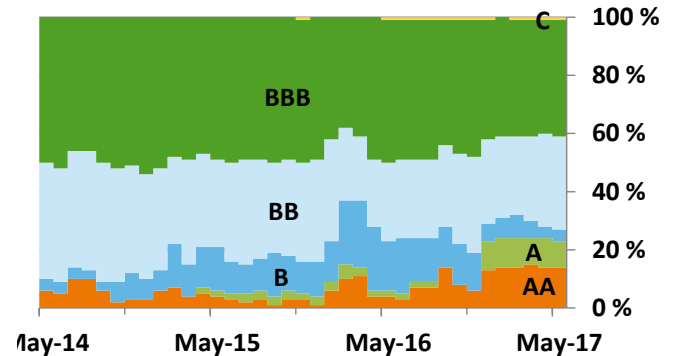
## 3Y Lower risk

Credit quality is one important element when looking at a corporate bond fund. A fund containing BBB or better rated companies will in the long run likely deliver a lower but more stable return than a fund with BB or lower rated companies. The two parameters of return and stability can be combined and expressed as a risk adjusted return. By doing this the best ratio is found in the mid segment of the rating scale. BBB-BB rated bonds therefore dominate the holdings in SKAGEN Credit. This has been the case since start and the recent risk reduction in SKAGEN Credit has reduced the proportion of B rated companies and increased the proportion of A rated companies.

The average rating in the fund has increased from BB to BBB over the last 12 months.

Another important element is the average time to maturity on the holdings (also known as spread duration or credit duration). This is simply a measure of how much the value changes when credit spreads change. The longer the bonds are, the greater a credit spread change will influence the fund's value. In SKAGEN Credit the holdings are shorter than the average bond.

The average time to maturity is currently only 2.3 years in SKAGEN Credit. It has been reduced by around one year over the past 12 months.

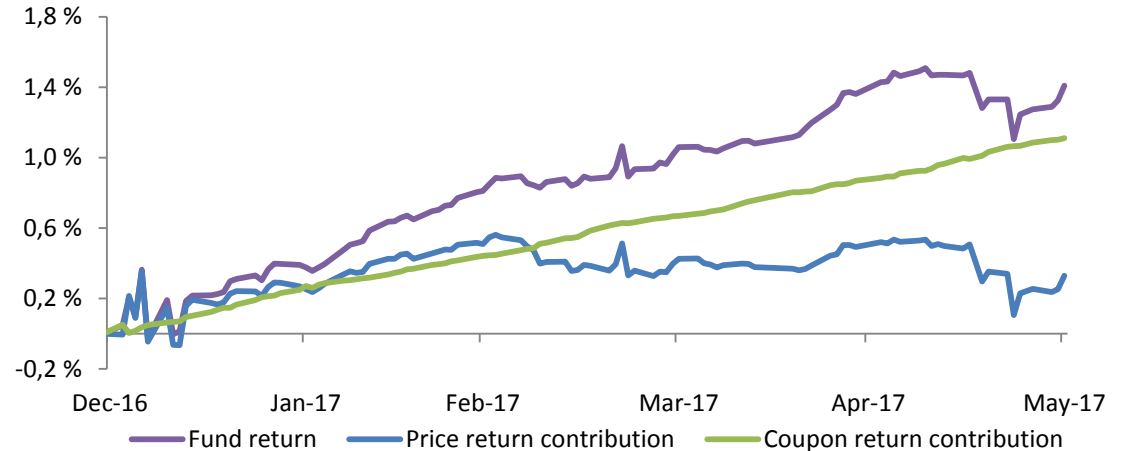


# 3Y The mandate

SKAGEN Credit has a rather unique mandate. It is a truly global corporate bond fund where the return and volatility are generated by bond coupons and changes in corporate bond spreads. Interest rate risk is reduced to a very low level and currency risk is reduced to a minimum.

The graph below shows the contribution for SKAGEN Credit NOK year to date. The same relative contribution applies to SKAGEN Credit EUR and SKAGEN Credit SEK, but the absolute return numbers are different.

As can be seen from the graph, the fund's return is a combination of a stable income from the bond's coupons, and market price changes of the same bonds.



SKAGEN Credit NOK YTD

# 3Y One big market

The global corporate bond market is huge and consists of both investment grade (IG) and high yield (HY) bonds. Even though it is a market with a lot of natural correlation there are some important differences.

The most obvious one is the difference in credit quality, where a strict line is drawn between BBB and BB ratings. Companies with BBB rating or better are IG and the remainder are HY. Fixed income investors are often bound to either IG or HY and very seldom have the mandate to invest in both.

## Developed vs. emerging markets

The corporate bond world has also been divided into developed and emerging markets. Unfortunately this does not say much about the real risk. “Emerging markets” consist of a range of different markets that do not necessarily correlate anymore than a developed and an emerging market do. Whether or not the categorisation is relevant, it is still in use and many investors have limitations on how much they can invest in emerging markets.



## Currency and geography

Another difference is currency. Many investors are bound to one currency and cannot choose others with a more attractive return. A related difference is the regional split, where investors are limited to a specific country (often their own) or a specific region.

These two differences combined are often visible when a company issues bonds both in its local currency e.g. CHF and in USD. The domestic bond has many local buyers but these investors are restricted to only investing in this bond due to either the currency or the geographical market where it is issued. Buyers of the USD bond are often located in another country (the US) and have less incentives/interest to invest in a foreign company.

### **Home bias**

Region-wise the corporate bond market is dominated by US and European companies. These two regions are also where most of the investors are based. Each country or region is often very local with mostly domestic investors. The few foreign investors they have often withdraw from the external markets quickly when anything happens, as the home bias effect is triggered in times of uncertainty. It simply feels safer to invest in your home market.

### **And the winner is...**

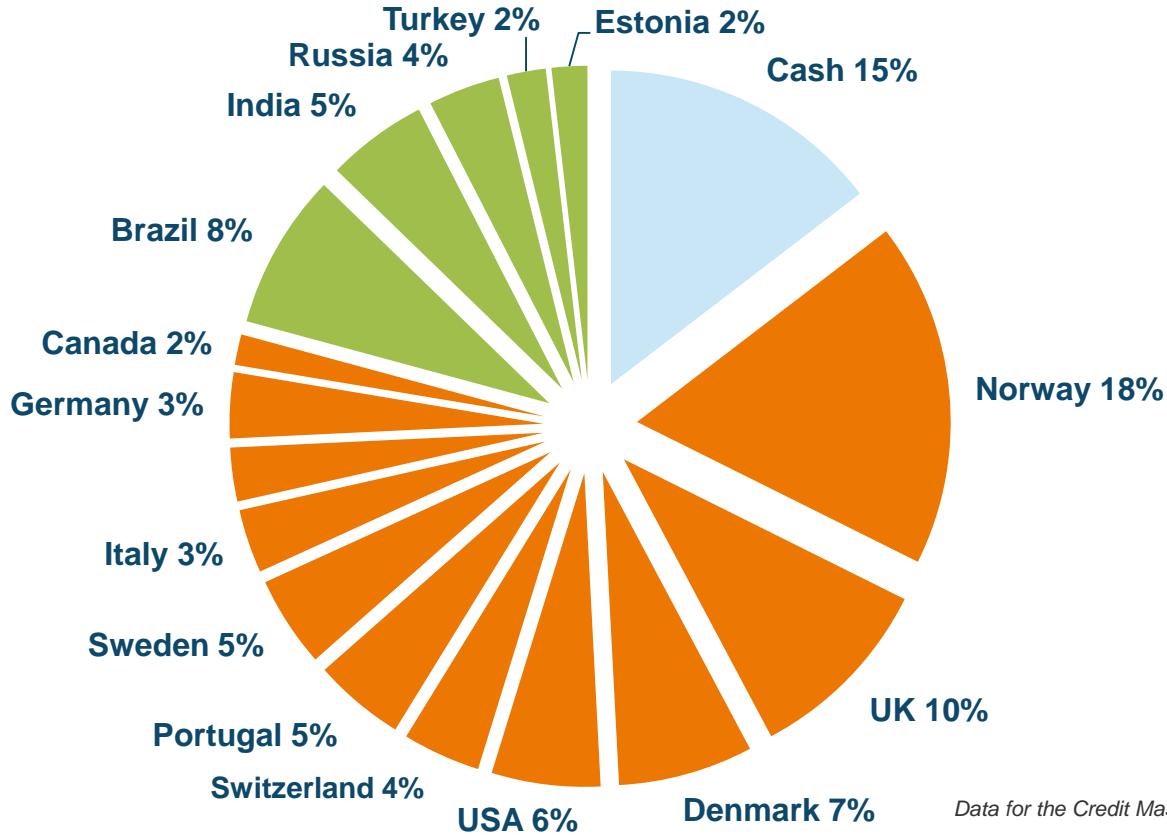
The way the whole corporate bond market works often provides attractive opportunities for the ones that aren't bound by rating, geography or currency. Funds with the mandate to freely pick bonds are rare. SKAGEN Credit is one of the lucky ones.



## SKAGEN Credit EUR A – Key numbers

Key numbers as of 31 May	SKAGEN Credit EUR A	Index (EURIBOR 3M)
Return last month	-0,1 %	0,0 %
Return year to date	0,6 %	-0,1 %
Return last year	4,2 %	-0,3 %
Return last 3 years (annualized)	0,7 %	-0,1 %
Return since inception (annualized)	0,7 %	-0,1 %
Duration	0,9	0,25
Time to maturity	2,3	N/A

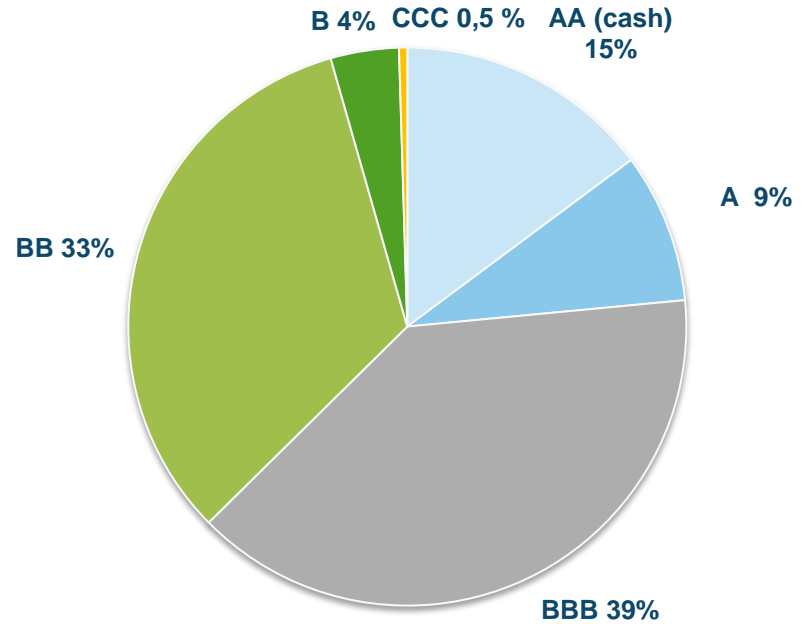
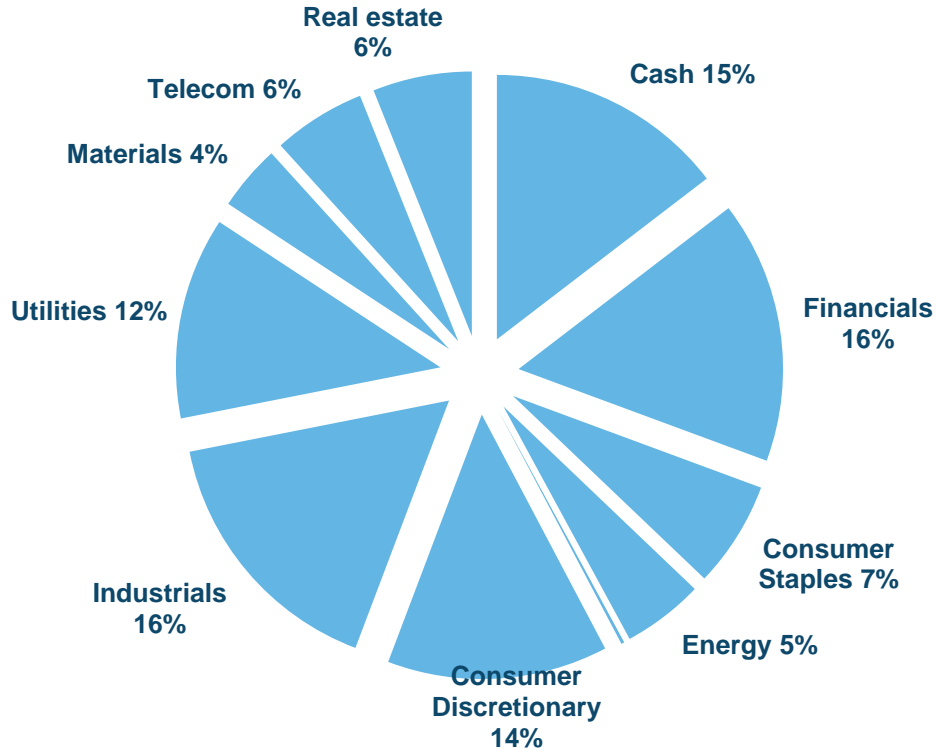
# Country diversification



Developed markets:	64 %
Emerging Markets:	21 %
Cash:	15 %

Data for the Credit Master fund

# Sector and credit rating distribution



Investment grade: 63 %

High Yield: 37 %

Average rating: **BBB**

Data for the Credit Master fund

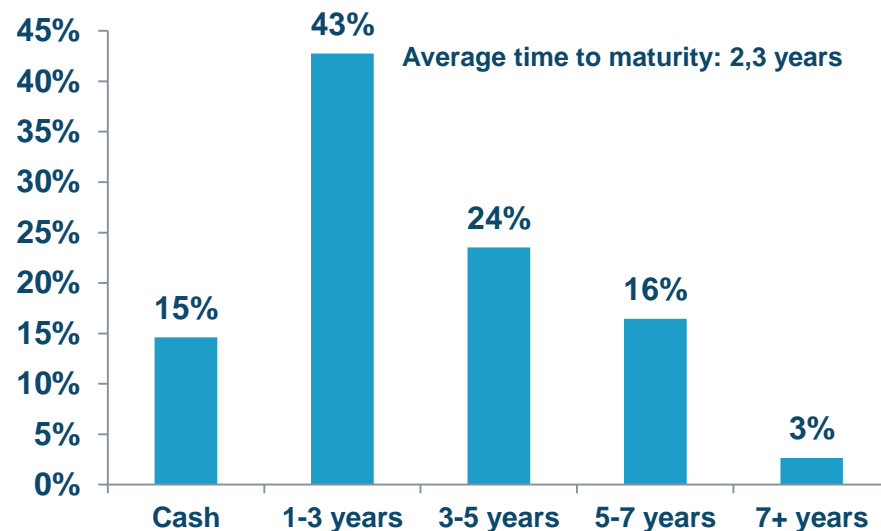
# Interest rate duration and time to maturity

## Interest rate exposure and denominated currency (before currency hedge)

Currency	Bond denominated	Interest rate duration
USD	44%	1,2 year
EUR	10%	0,5 year
GBP	19%	1,2 year
NOK	19%	0,2 year
SEK	3%	0,3 year
DEK	3%	0,2 year
Sum Fund	100%	0,9 year

Data for the Credit Master fund

## Credit exposure - time to maturity profile



## Top ten investments

Company	Country of risk	Credit rating*	Percent of fund
Energias de Portugal	Portugal	BBB-	4,7 %
Heathrow	United Kingdom	BBB	4,7 %
BKK	Norway	BBB	4,7 %
Sparebanken Telemark	Norway	A-	4,4 %
Glencore	Switzerland	BBB	4,0 %
Schaeffler	Germany	BB+	3,4 %
Fiat	Italy	BB-	3,3 %
DSV	Denmark	BBB	3,1 %
Bharti	India	BBB-	3,1 %
Cosan	Brazil	BB	3,0 %
<b>Sum top 10</b>			<b>37,7 %</b>

*Average bond rating.*

*\*\* Represent bonds from several legal units within the Glencore group*

*Data for the Credit Master fund*

# The SKAGEN Credit investment universe



**SKAGEN Credit picks bonds both from the investment grade and the high yield spectrum with a high risk adjusted return potential. Minimum 50% investment grade.**

## For more information please visit:

Latest [Market report](#)  
Information about [SKAGEN Credit EUR](#) on our website

Unless otherwise stated, all performance data in this report relates to class A units and is net of fees.

Historical returns are no guarantee for future returns. Future returns will depend, inter alia, on market developments, the fund manager's skill, the fund's risk profile and subscription and management fees. The return may become negative as a result of negative price developments. KIIDs and prospectuses for all funds can be found on our website.

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